

Understanding 2004 Legislation Essential to Authorized Agents

Authorized agents will need to change some of their administrative and reporting procedures to comply with newly passed legislation. Seven of the nine SDRS bills passed by the 2004 Legislature affect plan features such as participation costs, eligibility requirements, and the compensation basis for calculating benefits. By reducing costs in programs that have proven, over time, to be more expensive than

anticipated, the new laws will save SDRS hundreds of millions of dollars.

Authorized agents will play an indispensable role in implementing the legislation by:

- ▶ insuring that payroll programs are adjusted to comply with the new laws
- ▶ modifying their own procedures to reflect the changes

- ▶ educating members to help them understand how the new laws may affect individual situations

SDRS will revise its publications, update its Web site, and provide additional supportive material to communicate the changes in the law. As always, SDRS staff members will be available to answer authorized

continued on the following page ...

2004 Legislation Affecting Plan Provisions

TITLE	SUMMARY	AFFECTS CONTRIBUTION REPORT	AFFECTS BENEFIT CALCULATION	AFFECTS ELIGIBILITY
1 Final Average Compensation Caps (HB 1032)	Limits the amount of the lump-sum payment received at retirement that can be used to calculate a member's retirement benefit.	X	X	
2 Special Pay Plan (HB 1033)	Creates a program that eliminates or defers taxes on termination pay.	X	X	
3 Optional Spouse Benefit (HB 1034)	Increases the cost of purchasing optional spouse coverage by 4 tenths of 1 percent. The increase will allow the program to pay for itself.	X	X	
4 Cost to Purchase Credited Service (HB 1036)	Fully funds the cost to the system of credited service purchases.	X		X
5 Retire/Rehire (HB 1037)	Revises benefit payment and membership status of retired members rehired by an employer participating in SDRS, so that members who retire/rehire receive lifetime benefits comparable to those who do not.		X	X
6 Compensation Basis for Benefit Calculations (HB 1038)	Changes basis for calculating disability and survivor benefits to be consistent with basis for calculating retirement benefits.		X	
7 Eligibility Requirements (HB 1039)	Bases eligibility for vesting and disability benefits exclusively on contributory service. Purchased service will not apply.			X

agents' questions.

The chart on the preceding page summarizes the seven bills

and shows the program features they affect. The articles following in this issue of *UpDate* present

the bills' key components and the resulting changes. **UpDate**

1 New Caps Set for Final Average Compensation

Currently, increasing final compensation with a lump-sum payment just prior to termination can result in a retirement benefit that is not adequately supported by contributions. The cost of this practice is borne by all members, not just by those receiving expanded benefits. To address these costs, new legislation reduces the amount of termination pay that can be used to calculate a retirement benefit. The law also changes the definition of compensation to omit lump-sum payouts for unused sick or annual leave.

Reducing caps on the compensation used to calculate benefits

will be implemented in two steps:

1. On July 1, 2004, the maximum that compensation can increase in the last quarter of employment will drop from the current 125 percent to 115 percent of any prior quarter. The average pay in the last four quarters of employment will be limited to 110 percent of any prior quarter, down from the current 115 percent.
2. On July 1, 2005, both caps will be reduced to 105 percent. **UpDate**

1 Authorized Agents' **ACTIONS**

- » Inform members of the change in the basis for calculating benefits.
- » As of July 1, 2004, do not include lump-sum payouts for unused sick or annual leave in your report of a member's final compensation.

2 Special Pay Plan, Redefinition of Termination Pay Promise Savings on Taxes and Contributions

Members could receive substantial savings in their termination pay under a new plan authorized by the 2004 Legislature.

Rather than being paid directly to terminating members, qualified, end-of-career lump-sum payments will be deposited into a new retirement account, the Special Pay Plan. Operated like the SRP, the Special Pay Plan will offer members a variety of investment options. Members could withdraw their deposit soon after leaving employment, or use the account for retirement income. If members are in a lower tax bracket at the time of withdrawal than they are at

retirement, they could realize additional tax savings.

The Special Pay Plan will apply to all eligible SDRS members (age 55 or older and receiving at least \$2,000 in termination pay) whose employer elects to participate. State

government and the Board of Regents will be taking advantage of the plan beginning July 1, 2004. This spring SDRS will send all other SDRS employers the information they will need to enroll. **UpDate**

2 Authorized Agents' **ACTIONS**

- » Look for the information on the Special Pay Plan that SDRS will send out this spring.
- » Advise eligible members about the plan, enroll them before their final pay day.

3 Optional Spouse Coverage Rates Increase to Fund Benefits

Under new legislation, payments from members participating in the Optional Spouse Coverage will fully fund the program. The rate will increase by 0.4 of one percent of compensation, rising from 0.8 percent to 1.2 percent. The new rate applies to payrolls dated on or after July 1, 2004, even if the payroll includes time worked before July 1.

Other legislation will change the basis of compensation used to calculate optional spouse coverage. Through June 30, 2004, the basis will continue to be the highest one-year's compensation in the last three years. Effective July 1, 2004, the basis will be a member's final average compensation. **Up Date**

The new law does not change the rate for purchases contracted before July 1, 2004. Due to the anticipated volume of purchases, SDRS cannot guarantee the completion of purchase contracts requested after June 15, 2004. (Note that before requesting a contract, members must have past service verified.)

Service purchased before July 1, 2004, will continue to count toward vesting. Purchases contracted after that date will not. **Up Date**

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Authorized Agents' **ACTIONS**

- ▶ Advise your payroll or human resources personnel that after June 30, 2004, employer remittances to SDRS must consider the new rates.
- ▶ Inform participating members of changes. Increases in payments will be handled through the normal payroll deduction with no action required by members.
- ▶ Remind members choosing to withdraw from the program that their contributions are not refundable, and use Form E-2, *Notice of Enrollment Change*, to cancel participation.

4

Authorized Agents' **ACTIONS**

- ▶ Inform members that after June 30, 2004, rates for purchasing credited service will increase significantly.
- ▶ **Advise members who wish to purchase credited service to contact SDRS immediately.** If a prior employer must verify service, the process can be time-consuming. Verification must be completed before a contract can be written, and a contract must be written by June 30, 2004, to be governed by the old rates.
- ▶ Be prepared to explain why there is a multiple rate structure for purchases.

4 Increased Rates to Cover Costs of Purchasing Credited Service

New legislation will increase the rates for purchasing credited service so that those making the purchase will pay for its full cost. Rates will vary according to a member's age, with higher prices charged to older members whose payments have less time in the

system to generate investment earnings. For Class A members, the cost will range from 12 percent to 30 percent of pay. Because Class B members pay a higher contribution rate, the cost of purchasing credited service will also be greater, up to 45 percent of pay.



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5 Retired and Rehired Employees Will Enroll as New Members

A new law will even out the benefits of members who retire/rehire and those who do not. The law will:

- ▶ eliminate the cost of living adjustment (COLA) during reemployment
- ▶ treat rehired members as new hires
- ▶ calculate benefits earned during reemployment separately

rate from those figured at the initial retirement

The law makes a special provision for Class B Public Safety members who are rehired as Class A employees. They will continue to receive an annual COLA in their retirement benefit.

To be eligible under the current law, a retired/rehired member must be issued a paycheck in their new job before July 1, 2004. **UpDate**

6 All Benefit Calculations Made Uniform

Beginning July 1, 2004, SDRS will bring uniformity to the calculation of its retirement, survivor, and disability benefits. Currently the highest annual salary in the last three years is used to determine survivor and disability benefits. After the new law takes effect, survivor and disability benefits will use the same basis that retirement benefits use – final average compensation.

For those who become eligible for disability or survivor benefits after July 1, 2004, the new law may reduce benefits somewhat. Benefits will not change for those members and survivors who are receiving or qualify to receive benefits before July 1, 2004. In addition, the law will not affect the benefit of survivors of members who die after retirement. **UpDate**

5 Authorized Agents' ACTIONS

- ▶ Make sure members understand that they must receive a paycheck for reemployment prior to July 1, 2004, to qualify as retired and rehired under the current law.
- ▶ Remind members that they must meet the vesting

requirement of three years of contributory service as a rehired employee to be eligible for additional benefits.

- ▶ After July 1, 2004, enroll rehired employees as new hires, not as continuing members.

6 Authorized Agents' ACTIONS

Be aware of the change in the law. No specific action is required.

7 Only Contributory Service to Count Toward Vesting

A new member must accrue three years of contributory service to become vested in SDRS, according to a new law to take effect July 1, 2004. After that date, purchased service will no longer apply toward the three-year vesting or disability requirement.

Contracts to purchase service dated before July 1, 2004, are

governed by the old law, even if purchases have not been completed. Contracts requested after June 30, 2004, are governed by the new law, will be charged the new rates (as discussed in *Increased Rates to Cover Costs of Purchasing Credited Service*, page 3), and will not count toward vesting. **UpDate**

7 Authorized Agents' ACTIONS

Exclude credited service contracted for purchase after June 30, 2004, in determining a member's vested status or eligibility for disability benefits.